

Presentation

On



“Pakistan’s Economy and National Security ”

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Outline of Presentation

Why Economy Matters



What Makes National Security Weak?



Pakistan Economy in Historical Perspective



Why We have Landed in such a Difficult Situation?



Current Economic Challenges



What Needs to be Done?



Concluding Remarks

Why Economy Matters?

- ◆ There exists a strong linkage between the country's national security and the economy.
- ◆ Economy affects the lives of the people of Pakistan
- ◆ A strong economy can ensure strong defense; it will enhance country's power and hence will strengthen national security
- ◆ According to Paul Kennedy, "a nation's military strength rests on its economic strength"
- ◆ What is military strength? It is nothing but power. What is power? It is the ability to influence the behavior of others in accordance with one's aims and objectives
- ◆ Power can lead to prosperity and prosperity may generate more power
- ◆ Accordingly, in order to strengthen national security, a nation needs to possess economic security as well.

- ❖ According to Robert McNamara, “Security means development and without development there is no security”.
- ❖ Economic Backwardness generates violence, social conflicts political turmoil and weakens national security.
- ❖ A strong Economy also ensures political and social stability, which, in turn, makes the economy even more stronger
- ❖ A strong economy would ensure strong defense and not the other way round

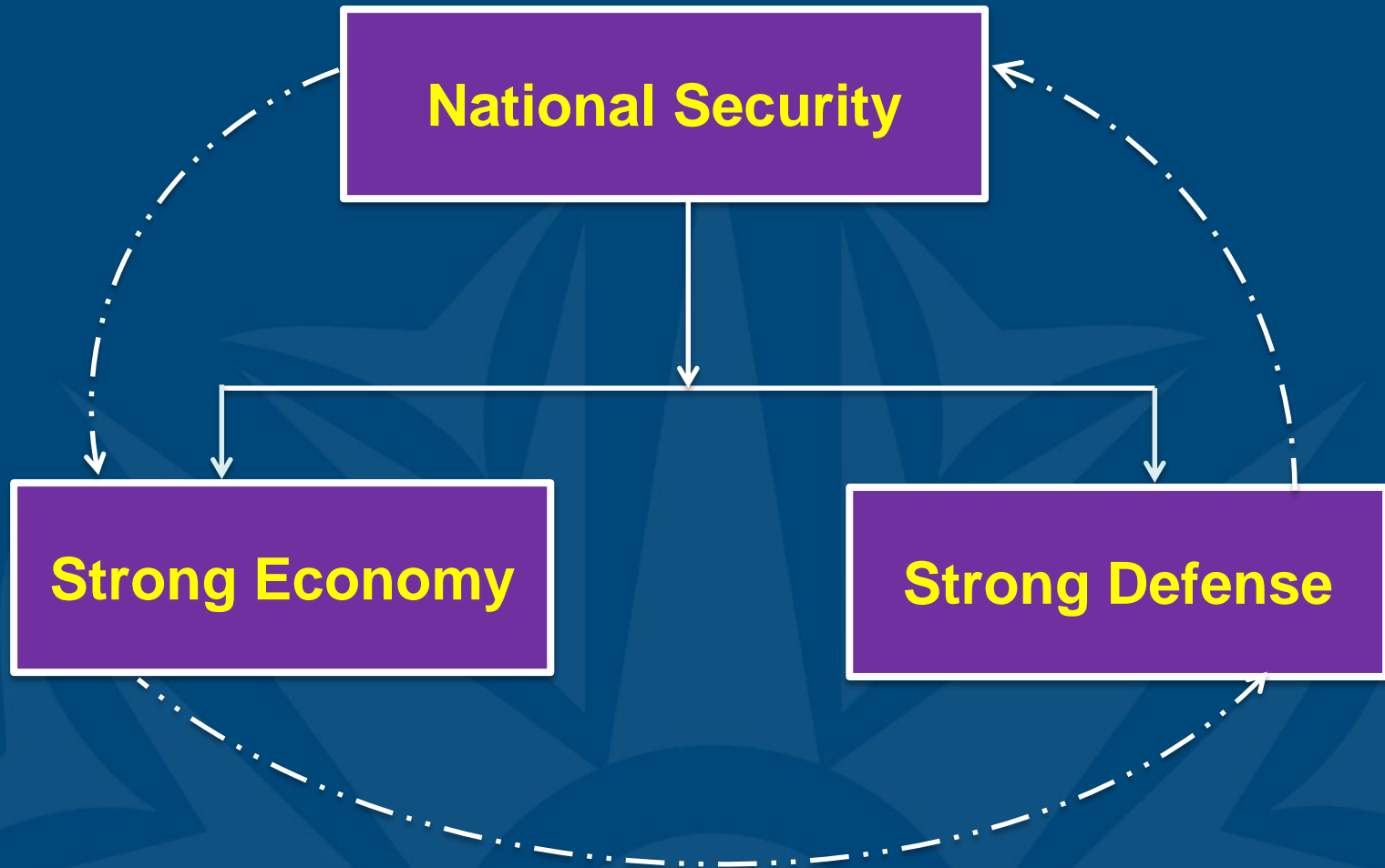
EXAMPLE FROM SOVIET UNION

PERIOD	REAL GDP GROWTH	DEFENSE SPENDING AS % OF GDP
1928-39	4.2	2.0*
1940-49	3.2	-
1950-59	7.1	9.0**
1960-69	4.3	14.5
1970-79	3.4	13.9
1980-89	2.7	15.4@

*1928 **1950 @ 1980-84

Source: William Easterly and Stanley Fisher, "The Soviet Economic Decline", **The World Bank Economic Review, Vol. 9, No. 3, September 1995, pp 341-371**

National Security and Economy



What Makes National Security Weak?

♦ Weak Economy:

It is characterized by

- ❖ **Slower Economic Growth** (Economy growing by 3.0 – 3.5% when country's population is growing by over 2.0% p.a)
 - It fails to create enough jobs, especially for new entrants
 - Higher Unemployment
 - Rising poverty
 - Growing civil unrest, social chaos, breakdown of law and order
 - It weakens national security

❖ Large Fiscal Deficit

- When economy grows at slower pace it fails to generate enough fiscal resources
- Expenditure continues to rise with the rise in population (Wagner's Law)
- Government resorts to large scale borrowing to meet expenditure requirements. In the process the country accumulates debt.
- Bulk of Resources (Borrowed and domestically raised) go to pay for past borrowing (interest payments)
- Little or no resources available to invest in people and invest in infrastructure
- The quality of human resources and infrastructure continue to deteriorate
- They are major constraints to economic growth and prosperity, hence weaken national security.

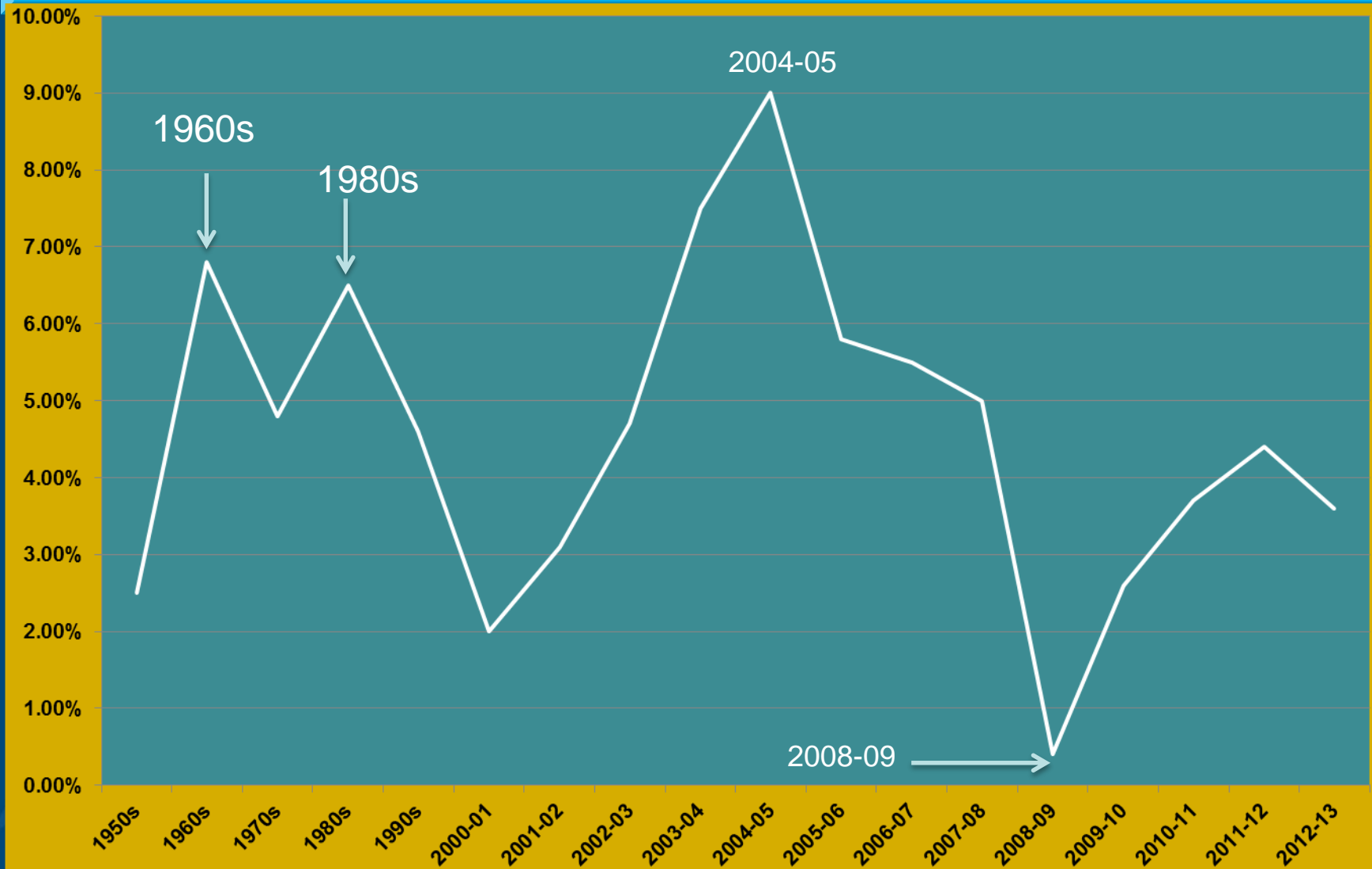
❖ **Persistence of Large Deficit Gives Rise to public debt and Balance of Payment Difficulties**

- A near bankrupt country goes to the IMF for bailout and loses financial and economic sovereignty
- A beggar has no foreign policy, it weakens national security.

Pakistan' Economy in Historical Perspectives

- ❖ Not withstanding numerous challenges that we faced over the last 66 yeas, Pakistan has done reasonably well on economic front. Pakistan's economy has grown at an average rate of 5.0% per annum over the last 66 years.
- ❖ Given its potential, Pakistan could have done better on economic front

Real GDP Growth (%)



Why have we landed in such a difficult situation since 2007-2008?

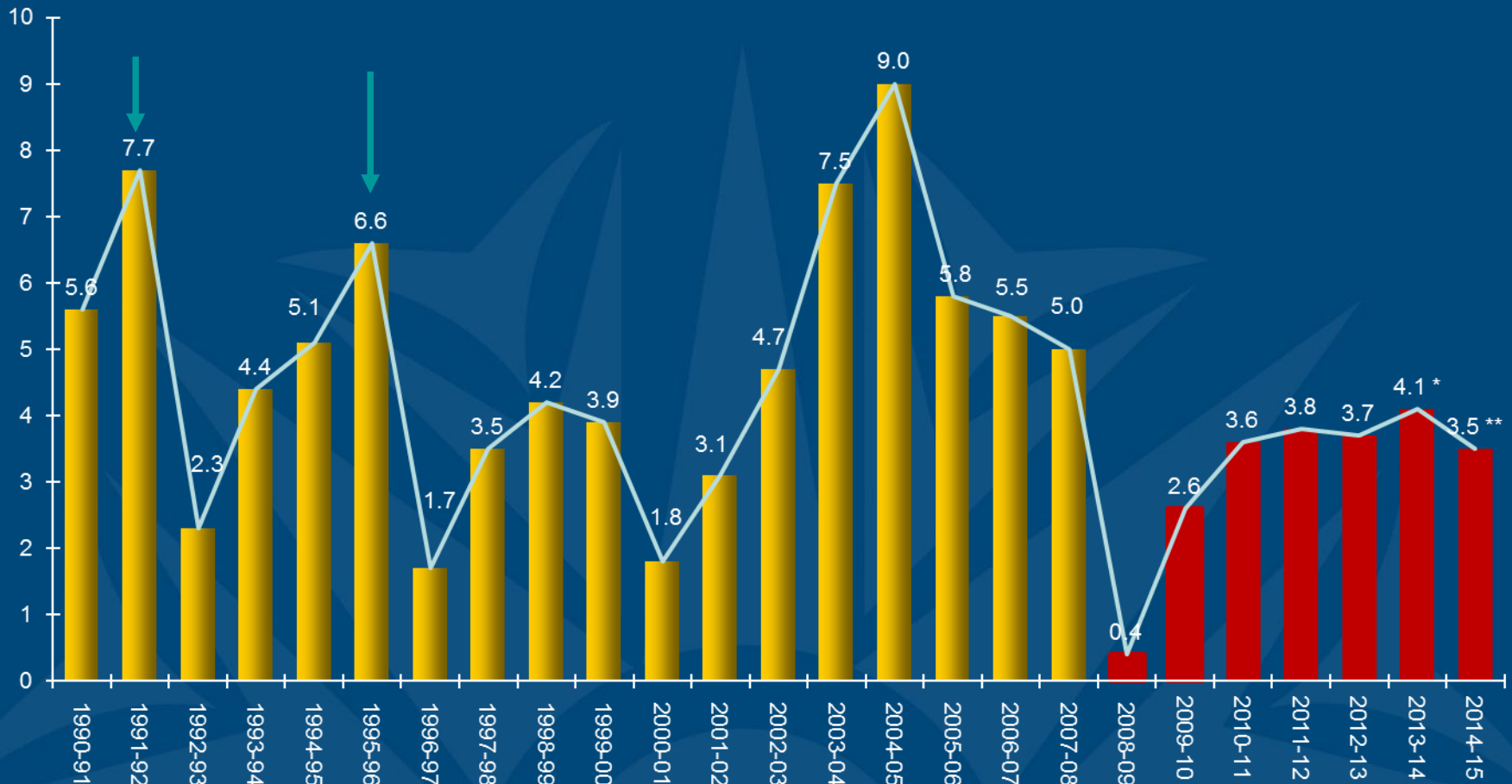
- ❖ Pakistan witnessed cataclysmic events unfolding on domestic and external economic scene
 - Food & Fuel Crisis of 2007-2008
 - Collapse of global economic and financial system in 2009-2010 (The Great Recession)
 - Intensification of war on terror
 - Deteriorating security environment
 - Absence of credible economic team
 - Height of fiscal indiscipline
 - Poor governance
 - Economy out of radar of the government
 - And most importantly, weak and non-serious leadership at the helm of affairs

Consequently

- ❖ Pakistan's economy has been damaged to the core
 - Key Economic Institution like Ministry of Finance, State Bank of Pakistan, Planning Commission and all the Regularity Bodies (SECP, OGRA, NEPRA, PEMRA etc.) have been severely weakened
 - Economic growth slowed to an average of 3.0% per annum over the last six years from an average of almost 7.0 per annum during the previous five years (2002-07)
 - Investment down to 50 years low at 12.5% of GDP from as high as 22.5% of GDP only five years ago
 - Domestic Saving Rate at 5.8% of GDP is the lowest in the country's history from an average of 15% of GDP during the previous five years
 - Large – scale manufacturing growth averaged 0.7% per annum over the last five years from an average of 12.4% per annum during the previous five years

- Budget deficit averaged **7.0%** of GDP, reaching as high as **8.8%** in 2012-13
- Public debt **tripled in 6 years** from Rs. 5 trillion in 2007 to Rs. 15 trillion in 2013
- Over **\$25 billion** external debt added in **6 years**
- Foreign Investment has simply collapsed – down from **\$8.5 billion in 2007** to just **\$1.6 billion** in 2013
- Inflation persisted in double digits for more than **50 months** in a row
- Pak Rupee has lost **42%** of its value since 2007
- Poverty and Unemployment have increased
- PSEs are bleeding and consuming over **Rs. 400 billion annually**
- Power Sector has received **Rs. 2000 billion in subsidy** in the last five years

Real GDP growing at an average rate of 3.1% p.a during the last six/seven years

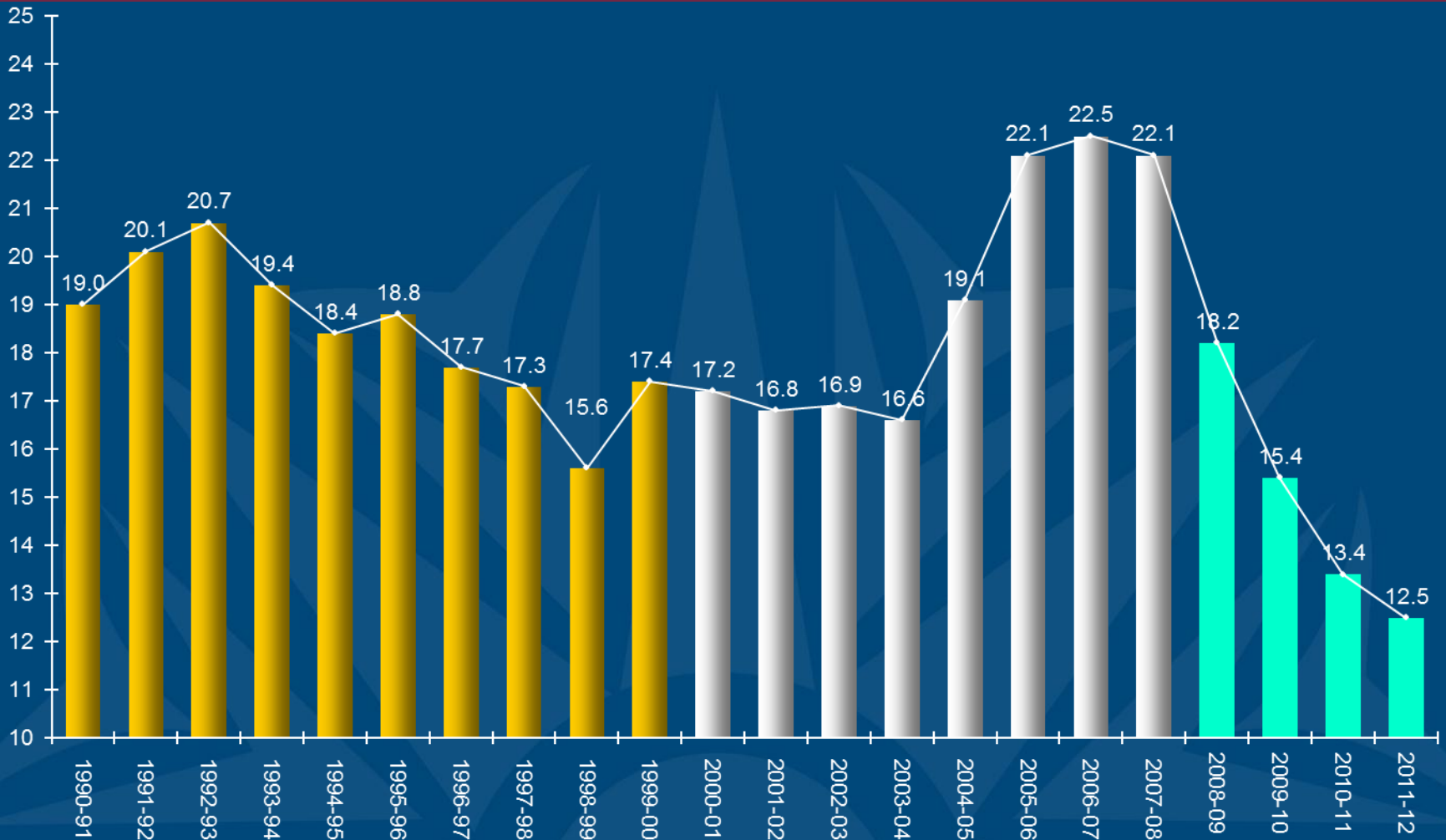


* Highly controversial ** Projected

Source: Various Issues of Economic Survey

Investment Nosedived After 2007-08

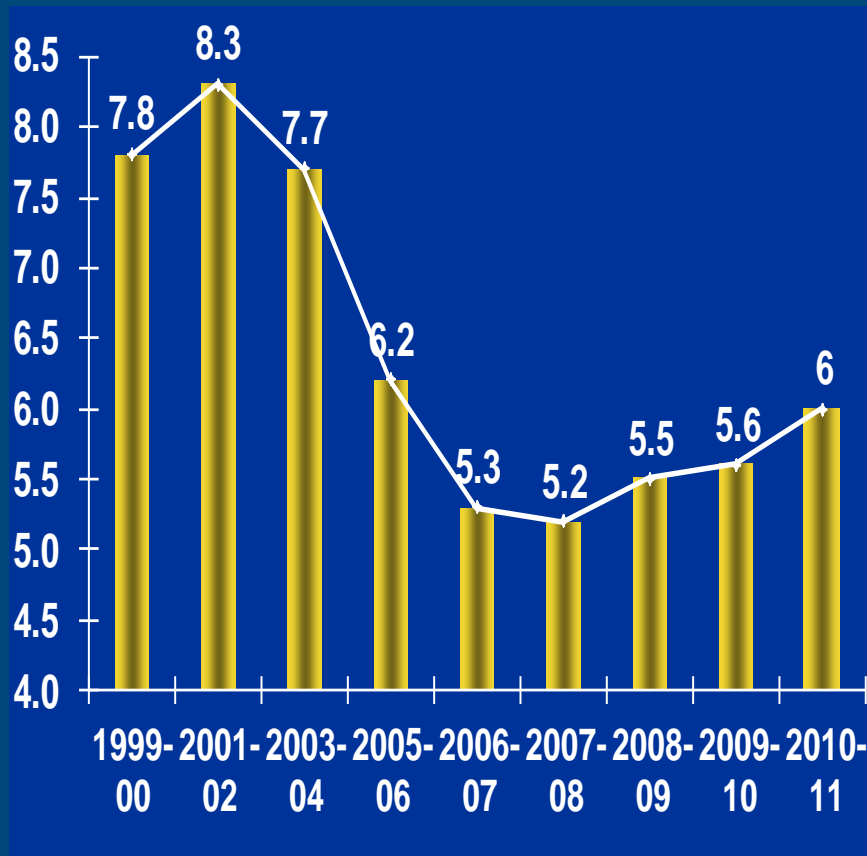
(as % of GDP)



Source: Various Issues of Economic Survey

Unemployment is Rising

Unemployment rising...



Source: Economic Survey 2006-07

Pace of job creation slowed in recent years

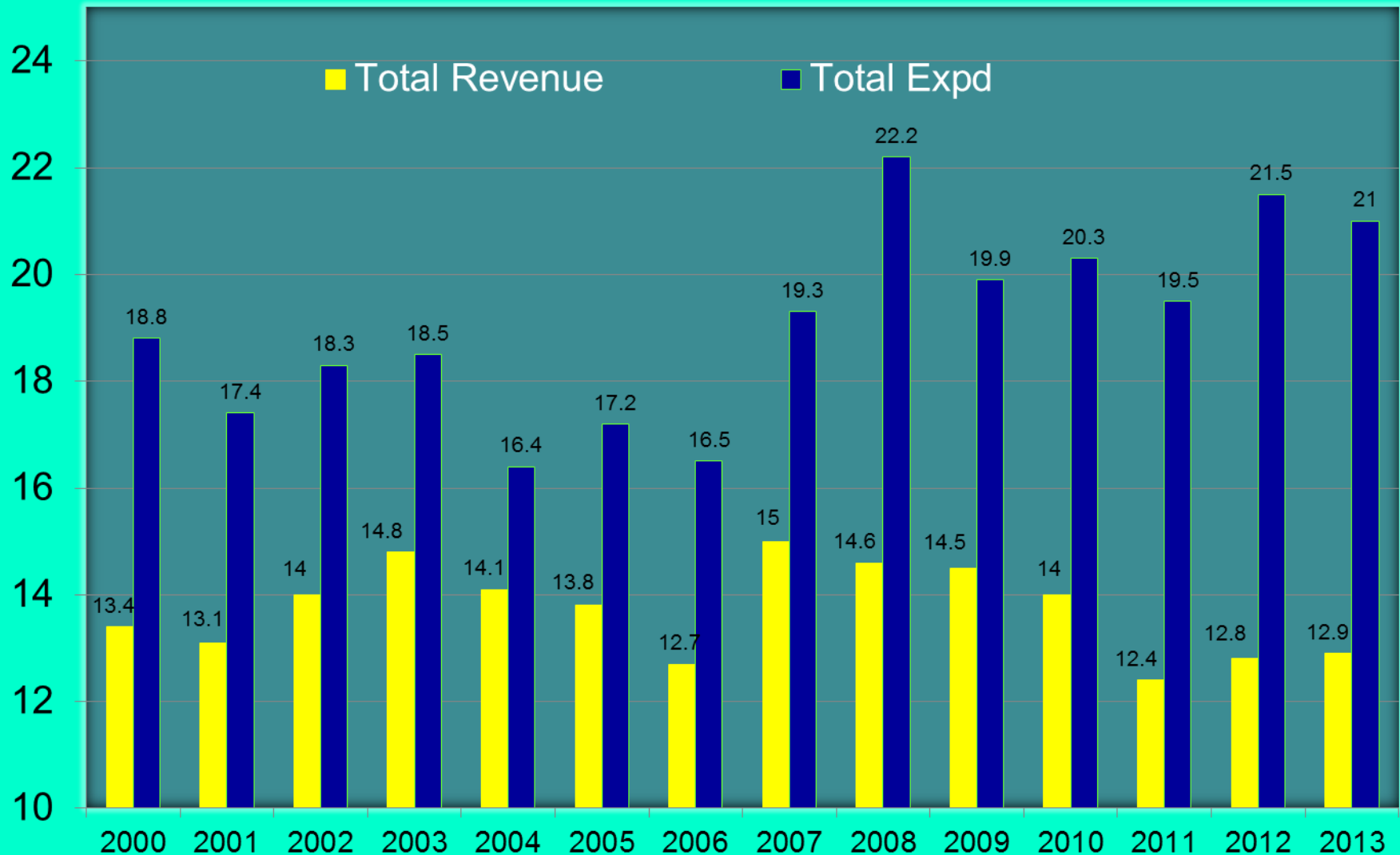
Labour Force Survey	Employment (in millions)	Number of New Employment (in millions)
FY 97	35.16	-
FY 00	37.22	2.06
FY 02	39.45	2.23
FY 04	42.42	2.97
FY 06	47.37	4.95
FY 07	48.07	0.7
FY 08	49.52	1.45
FY 09	52.71	3.19
FY 10	54.05	1.34
FY11	55.17	1.12
FY 12	55.80	0.63
FY 13	56.58	0.78

We need to create 3.5- 4.0 million jobs per year in the next 10 years for new entrants

Source: Labour Force Survey, FBS

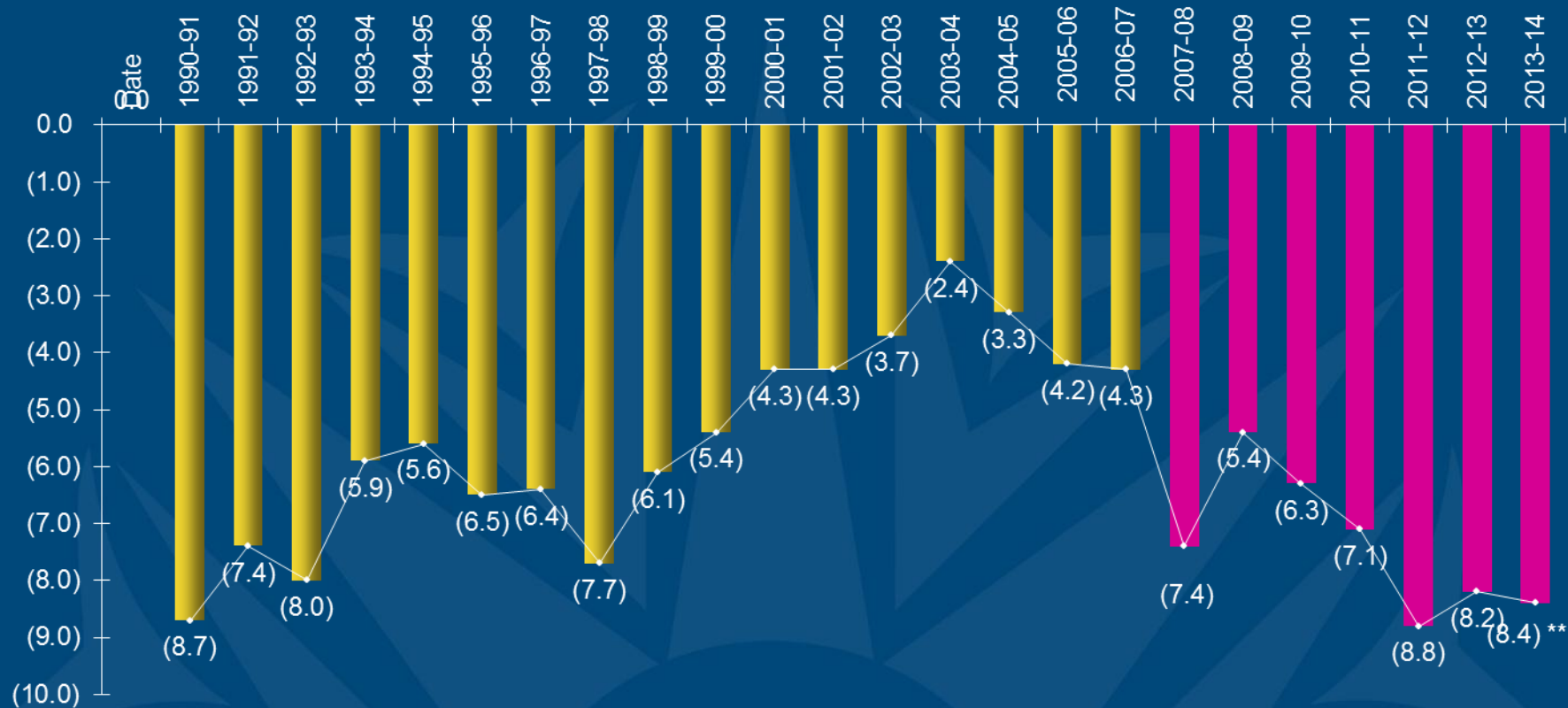
Trends in Revenue and Expenditure

(as % of GDP)



Pakistan sustained a very large budget deficit During 2008-14

Overall fiscal deficit (% of GDP)



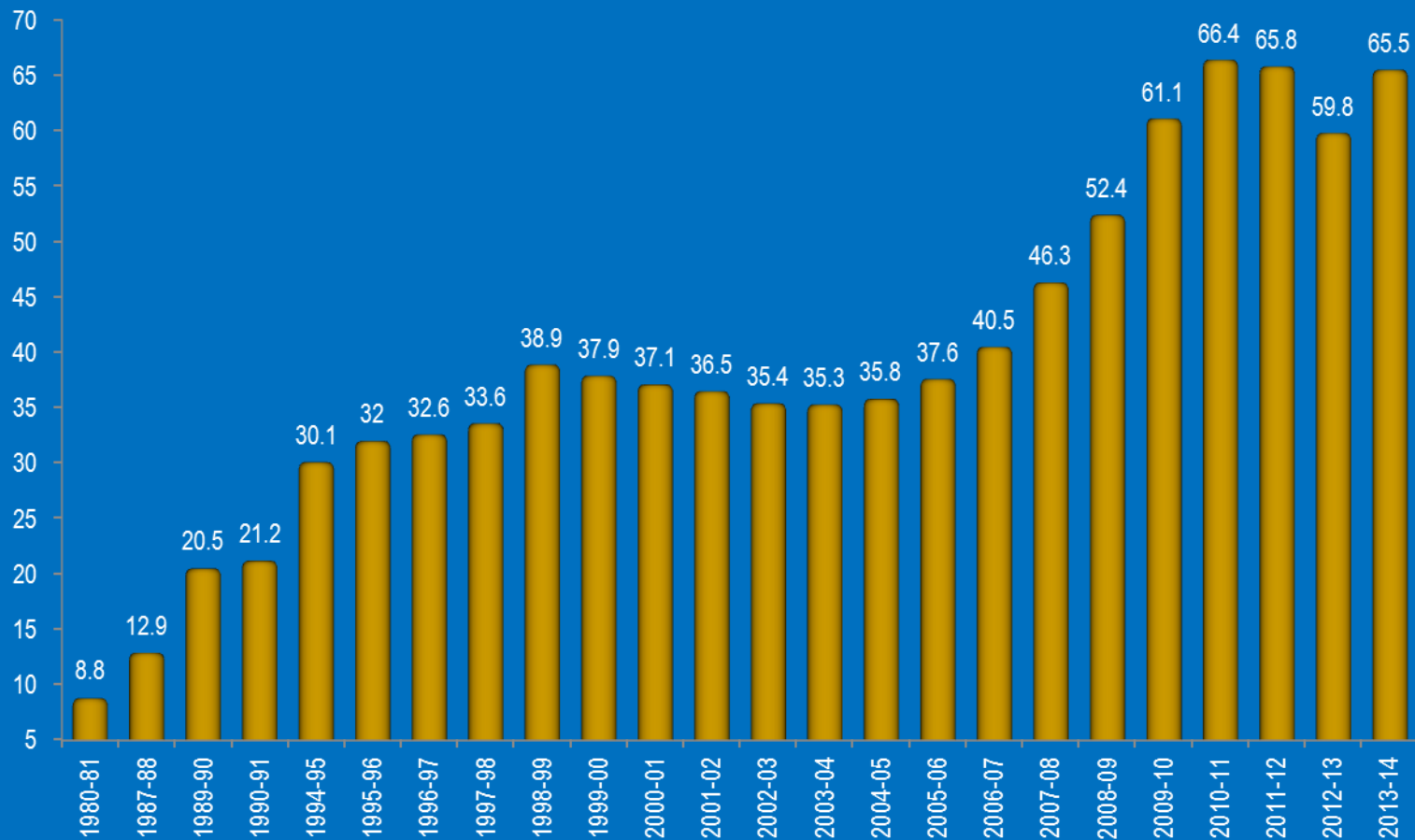
* Including earthquake related expenditure

** My calculation

Source: Ministry of Finance

Trends in External Debt and Liabilities

External Debt and Foreign Exchange Liabilities (Billion \$)



Pakistan's Debt Profile Since Independence

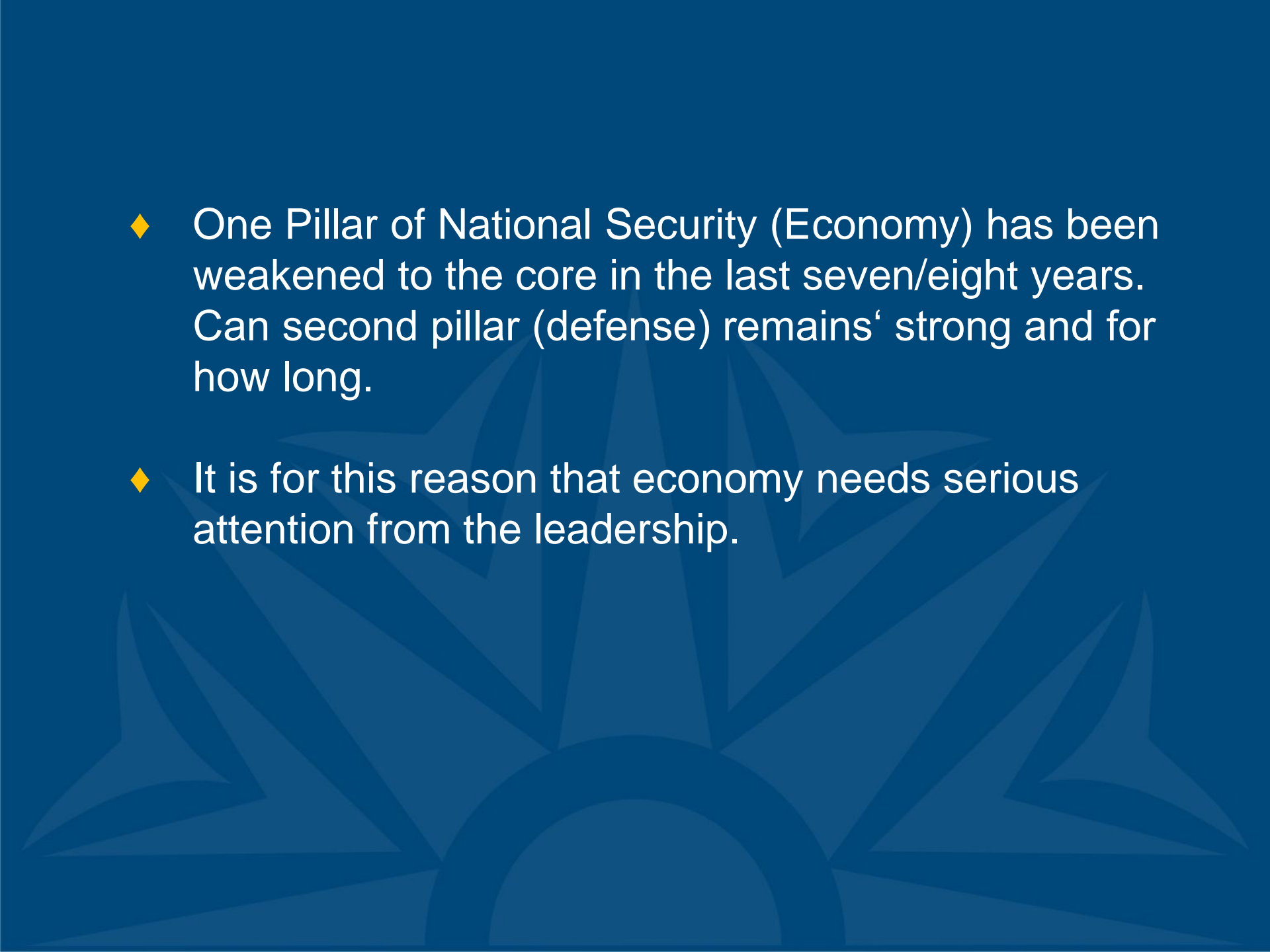
Period	External Debt & Liabilities (Million \$)	Public Debt (Billion Rs)
1947-48	0.0	-
1949-50	0.0	-
1959-60	145.0	-
1969-70	2959.0	-
1979-80	9458.0	155.4
1989-90	19207	801.2
1999-2000	37860	3018
2006-07	40500	4814
2009-10	57600	8911
2013-14	65,533	15,924

Source: State Bank of Pakistan and Debt Office, Ministry of Finance

Changes in Debt Profile

Period	External Debt & Liabilities (million \$)	Public Debt (Billion) Rs)
1948-60	145	-
1960-70	2814	-
1970-80	6499	155.4
1980-90	9749	646
1990-2000	18653	2217
2000-2007	2640	1796
2008-2014	25,033	11110

Note: Pakistan accumulated \$43.686 billion (or 67%) external debt and liabilities in the decade of the 1990s and in the last seven years. In other words , 2/3rd accumulation of debt took place in 17 years and 1/3rd (\$21.847 billion) and 1/3rd in the remaining 49 years.

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- A stylized sunburst or starburst pattern in shades of blue, centered behind the text. The pattern consists of multiple triangular rays emanating from a central point, creating a sense of radiance and focus.
- ◆ One Pillar of National Security (Economy) has been weakened to the core in the last seven/eight years. Can second pillar (defense) remains' strong and for how long.
 - ◆ It is for this reason that economy needs serious attention from the leadership.

Current Economic Challenges

- ◆ Large – Scale Manufacturing growth has slowed to 2.6% in July – December 2014 as compared with 6.5% in the same period last year
- ◆ FBR tax collection has collapsed in January 2015. Tax collection was up by 4.5 percent in January 2015.
- ◆ This growth in tax collection was achieved by holding back refund. If refund was assumed to be of last years level, the January 2015 tax collection was up by only 1.1%
- ◆ Tax Collection during July – January 2014 -15 was up by 12.4 percent as against the required growth of 24.0 percent for the year

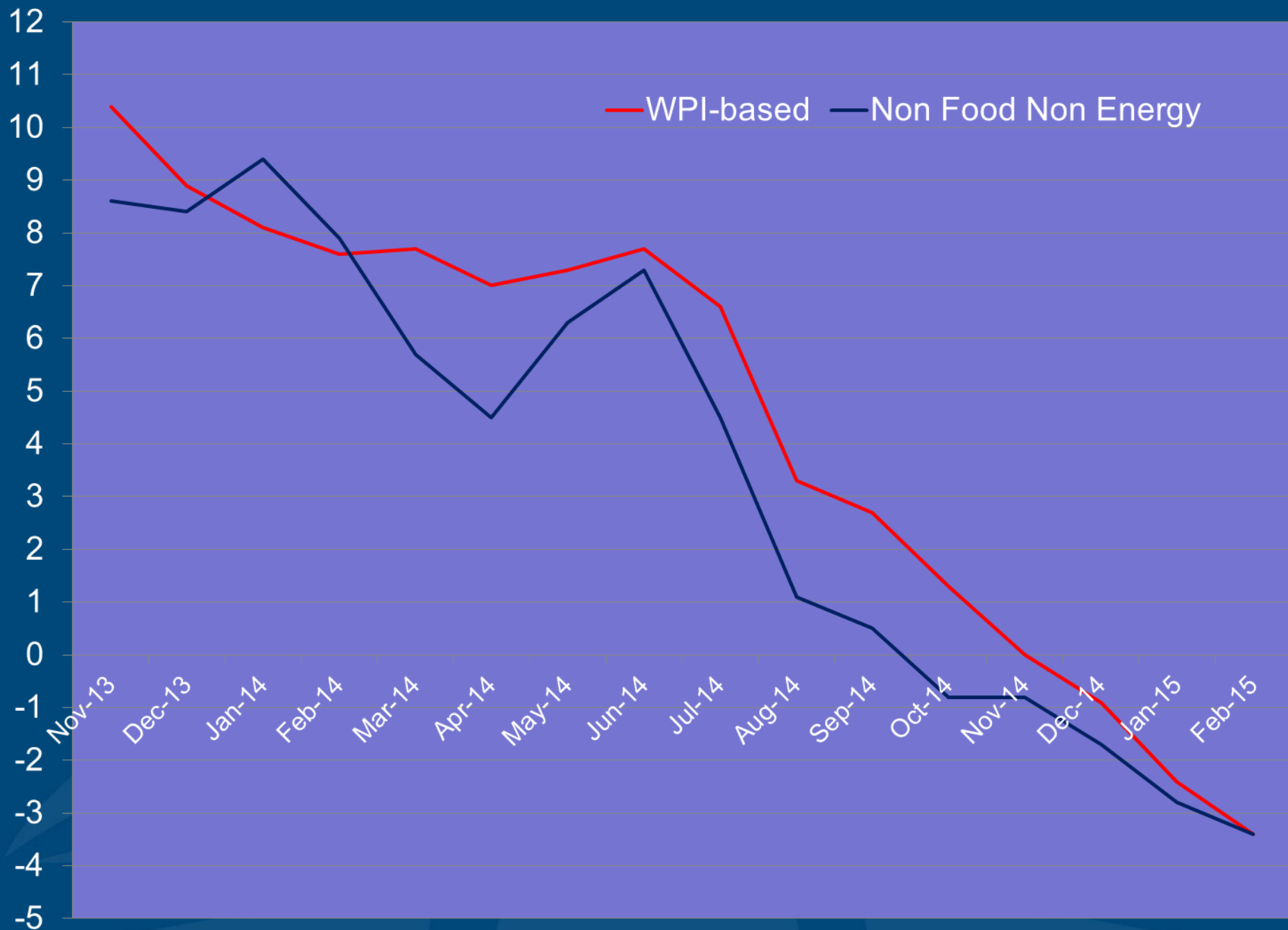
- ◆ Tax Collection target has been revised downward twice: From Rs 2810 billion to Rs 2756 billion to Rs 2691 billion
- ◆ Even to achieve Rs. 2691 billion target, FBR would need to collect Rs. 1346 billion in the remaining 5 months (Feb-June). In other words tax collection must grow at an average rate of 26 percent during the next five months.
- ◆ The twice revised target will not be achieved. The FBR, at best, would collect in the range of Rs. 2550-2570 billion 2014-15 – a slippage of Rs. 240-260 billion.
- ◆ Massive shortfall in revenue despite additional tax measures of Rs. 391 billion-Rs. 231 billion at the time of budget and Rs. 160 billion through several mini budget

- ◆ The performance of sales tax thus far has been pathetic. Domestic sales tax collapsed in January 2015-down by 12 percent. During July-January, domestic sales tax declined by 0.2 percent. This is a clear indication of the slowing economy/slowing demand.

- ◆ Pakistan's economy landed in deflation. Whole sale price index (WPI) based inflation is continually declining-from 6.6% in July 2014 to zero percent in November 2014 to – 3.4 percent in February 2015.
- ◆ Non-Food Non energy inflation (WPI-based) has also entered in negative zone in October 2014. It was negative 3.4% in February
- ◆ Signs of deflation
 - negative inflation
 - collapse of domestic demand (sales tax collection at domestic stage has collapsed)
 - Private sector borrowing from commercial banks declined to Rs.140 billion during July-February 2014-15 as against Rs. 281 billion borrowing in the same period last year.

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- A stylized sunburst or starburst graphic in shades of blue, centered at the bottom of the slide. It features a semi-circular base from which multiple pointed rays emanate upwards and outwards, creating a fan-like shape.
- ◆ Industrial growth slowed to 2.6%
 - ◆ Exports have declined by 4.5 percent during July-January 2014-15. exports are down by 13 percent in February 2015.

- ◆ Pressure on budget can be viewed from the fact that the government borrowed Rs. 1.0 trillion from commercial banks as against Rs. -185 billion in the same period last year.
- ◆ Because of the pressure from the IMF the government has shifted its borrowing from the SBP to commercial banks.
- ◆ Foreign exchange reserves crossed \$ 10.5 billion- almost \$ 1.5 billion more than the level attained in end – June 2014. During this period, the net external borrowing is estimated at \$ 2.5 billion. Therefore, Forex reserves were up by US \$ 1.5 billion and the remaining \$ 0.9 billion was used to finance balance of payments deficit.



What Needs to be Done?

- ◆ Strengthen Economy to Strengthen National Security
- ◆ How can we Strengthen Economy
 - Through Good Macroeconomic Policies
 - Wide – Ranging Structural Reforms
 - Investment in People
 - Investment in Infrastructure
- ◆ We are living in a globalized world – a highly competitive world. Labour and capital have been the traditional factors of production.
- ◆ It is no longer valid today. A nation cannot progress with labour and capital in a knowledge – based global economy.
- ◆ It is not labour and capital but **quality of labour** and **quality of infrastructure** along with good macroeconomic policies that will help attain higher and sustainable economic growth, will bring economic prosperity and will strengthen national security.

- ◆ The most important resource in any country is its human resources. Pakistan is fortunate to be the sixth most populous country in the world having large share of young population. This young generation has the potential to become the guarantor of the national security.
- ◆ The average age of Pakistani population is 22 years
- ◆ We have 190 million population with 54% are below the age of 19 years and 63% below the age of 24 years.
- ◆ According to Population Council, Pakistan's population is projected to be 302 million by 2050; 163 million will be below the age of 19 and 190 million below the age of 24 years.

- ◆ Unless these young people are given access to quality education and health and livelihoods, they have the potential to become fodder for social and political explosion – a major threat to national security.
- ◆ How can a country transform its human resources into human capital? It can be done through the effective inputs of education and health.
- ◆ Human capital is an effective instrument for promoting economic growth and human capital is directly related to human development
- ◆ Thus, Human resources \Rightarrow human capital \Rightarrow human development \Rightarrow economic development \Rightarrow economic prosperity \Rightarrow national security.

Concluding Remarks

- ◆ Strong linkages exist between economy and national security
- ◆ Chain of causation runs from economy to defense to national security
- ◆ A weak economy cannot sustain strong defense and hence weakens national security
- ◆ Country needs to strengthen its economy through good macroeconomic policies, structural reforms, investment in education and health, and infrastructure.
- ◆ We need a strong economic team
- ◆ There is no dearth of good people in the country
- ◆ What is required is honest, competent and patriotic leadership providing full support to economic team
- ◆ We have the capacity to turnaround the economy in three years
- ◆ The country has faced serious challenges in the past but we recovered
- ◆ We have the capacity to recover from the ground zero once again, Inshallah

The background of the slide is a solid dark blue. In the lower half, there is a large, stylized sunburst or starburst graphic. It consists of a semi-circular base at the bottom, from which numerous triangular rays of varying lengths and shades of blue radiate upwards and outwards, creating a sense of light and energy.

Thank You